United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

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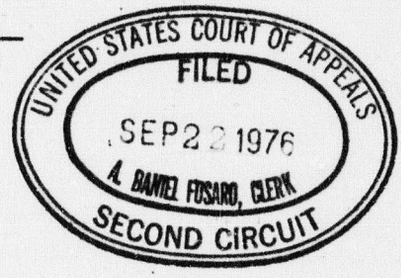

In re

INTERSTATE STORES, INC., et al.,

Debtors,

IRVING SULMEYER, as Receiver for the Estate of ESGRO, INC., a Debtor in Chapter XI,

Plaintiff-Respondent-Appellant,

-against-

JOSEPH R. CROWLEY and HERBERT B. SIEGEL, as Reorganization Trustees for WHITE FRONT STORES, INC., et al.,

Defendants-Appellants-Appellees.

On Appeal from the United States District Court
For the Southern District of New York

BRIEF OF APPELLANT IRVING SULMEYER,
RECEIVER FOR THE CHAPTER XI
ESTATE OF ESGRO, INC.

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Issues Presented

The issues presented by the appeal at bar are:

1. Did the United States District Court for the Southern District of New York ("District Court") err in determining that the Bankruptcy Court committed an abuse of discretion by authorizing the continued prosecution of a pre-Chapter X pending action in the California State Court involving White Front Stores, Inc., one of the Chapter X debtors?

2. Is the difference between a trial date of November 29, 1976 in the California State Court as compared to October 18, 1976 in the Bankruptcy Court of such magnitude to deprive Appellant of the right to jury trial and determination of all issues in the California Lawsuit by a court which is not involved in any aspect of the reorganization of White Front Stores, Inc., et al., under Chapter X of the Bankruptcy Act?

Statement of the Case

The instant appeal concerns the exercise of discretion by the Bankruptcy Court in respect of the conduct of litigation involving a debtor's estate. The precise issue pertaining to this appeal is whether the Bankruptcy Court's modification of the stay of actions incidental to the commencement of a reorganization case under Chapter X of the Bankruptcy Act, 11 U.S.C. §§ 506, et seq., constituted an abuse of discretion. The modification was granted after trial by Bankruptcy Judge Edward J. Ryan. The Chapter X case of White Front Stores, Inc., had been generally referred to Bankruptcy Judge Ryan by the District Court shortly after it was filed with its parent and affiliated corporations.

The modification of the stay granted by Bankruptcy Judge Ryan enabled the continued prosecution of an action entitled "White Front Stores, Inc., et al., Plaintiffs, v. Esgro, Inc., et al., Defendants; Esgro, Inc., et al., Cross-Complainants, v. White Front Stores, Inc., et al., Cross-Defendants, Case No. C50105 (the "California Lawsuit"), which had been commenced in the Superior Court of the State of California, County of Los Angeles ("California Court") on February 15, 1973. (A20, 33, 320).*

* Numbers in parenthesis preceded by "A" refer to the joint appendix.

The primary plaintiff in the California Lawsuit, White Front Stores, Inc., is one of the Chapter X debtors and at the time of the commencement of the California Lawsuit was engaged in business primarily in the State of California, operating and managing retail stores. The California Lawsuit initiated by White Front Stores, Inc., asserts 208 causes of action and seeks damages totalling approximately $879,000. (A20, 320). Subsequent to the commencement of the action and after joinder of issue, demand for jury trial and assertion of cross-complaints, the prosecution of the California Lawsuit was stayed because of (a) the filing by Esgro of a petition under Chapter XI of the Bankruptcy Act, 11 U.S.C. §§ 701, et seq., with the United States District Court for the Central District of California on March 13, 1973* and (b) the filing by White Front Stores, Inc. of a petition pursuant to Chapter XI of the Bankruptcy Act, 11 U.S.C. §§ 701, et seq., together with its parent corporation, Interstate Stores, Inc. and other affiliated corporations with the District Court in New York on May 22, 1974.** (A34-35).

On May 11, 1976, Irving Sulmeyer, as receiver for

* The stay in the Chapter XI case extended from March 19, 1973 to May 7, 1973 when the California Bankruptcy Court authorized Esgro, Inc. and its receiver to defend the California Lawsuit and assert any and all claims for affirmative relief (A320).

** Thereafter, and on June 13, 1974, White Front Stores, Inc., together with its parent and other affiliated companies filed amended petitions pursuant to Chapter X of the Bankruptcy Act, 11 U.S.C. §§ 506, et seq.

Esgro, Inc. appointed in the Chapter XI case in California (hereinafter sometimes collectively referred to as "Esgro"), the Appellant herein, initiated an adversary proceeding in the Bankruptcy Court, pursuant to the Rules of Bankruptcy Procedure, against Joseph R. Crowley and Herbert B. Siegel, the Chapter X Reorganization Trustees appointed for Interstate Stores, Inc. and its affiliates, including White Front Stores, Inc. ("Trustees"), the Appellees, to modify the stay of actions and allow the continued prosecution of the California Lawsuit. (A15-29).

Consistent with the provisions of Chapter X Rule 10-601, 421 U.S. 1069 (1975), the Bankruptcy Court gave precedence to the consideration of the adversary proceeding and on May 21 and 26, 1976, the trial of the proceeding was conducted before Bankruptcy Judge Ryan. After consideration of the evidence and testimony adduced at that trial which established that: (a) many of the witnesses having personal knowledge of the facts material to the California Lawsuit reside in California (A56, 77-80); (b) parties to the California Lawsuit were not subject to the jurisdiction of the Bankruptcy Court (A57, 207); (c) a trial of the Trustees' objection to the allowance of the claim of Esgro filed in the Chapter X case would not completely resolve all of the issues raised in the California Lawsuit and would leave unresolved the Trustees' principal claims in the California Lawsuit (A164); (d) the issues involved in the California Lawsuit

action and cross-action were closely intertwined (A112-114, 164-165, 225); (e) California state law governed the issues between the parties (A56); and (f) a trial by jury was available to the parties in the California Court (A140); the Bankruptcy Court by order dated May 26, 1976 modified the stay of the prosecution of the California Lawsuit but required the parties to report back to it "on or before July 8, 1976" as to the progress of discovery and the result of an application to the California Court for an order advancing the trial date of the California Lawsuit. (A323).

The latter provision was in response to the only contention and defense offered by the Trustees in the adversary proceeding, i.e., the prosecution of the action and cross-action in the California Court before a jury would delay a determination of the $38,000,000.00 claim filed by Esgro against White Front Stores, Inc. (A150-151, 154-156). Thereafter, pursuant to provisions of the order of May 26, 1976, it was reported to Bankruptcy Judge Ryan that in accordance with the agreement made between counsel for Esgro and the Trustees, the trial of the California Lawsuit had been set down for November 29, 1976.

Notwithstanding the accelerated trial date granted by the California Court, the Trustees thereafter attempted a number of maneuvers to circumvent the relief granted by

the Bankruptcy Court. (A335-345, 389-398). Their efforts were to no avail and based upon the facts, the Bankruptcy Court adhered to its findings and conclusions that the prosecution of the California Lawsuit in the California Court was for the convenience of the parties and potential witnesses and in the best interests of justice. (A387-388, 482-486). The last determination made by the Bankruptcy Court is represented by the order of July 23, 1976 denying the application of the Trustees to fix the time of trial of the "application to expunge claim***" of Esgro. (A482-486). The Trustees filed an appeal from that order to the District Court. (A487-488). After an expedited hearing and on September 1, 1976, District Judge John M. Cannella rendered his opinion and order reversing the Bankruptcy Court on the basis that it had abused its discretion in modifying the stay of actions. (A503-506). The District Court reinstated the stay of the California Lawsuit. (A504). In addition, District Judge Cannella (a) withdrew the general reference of the Chapter X cases to Bankruptcy Judge Ryan, in respect of the Esgro claim; (b) fixed a trial date of October 18, 1976 for the Trustees' objection to the Esgro claim; and (c) directed that all pre-trial discovery be completed by September 27, 1976. (A504-506).

The order of the District Court adopts in full the arguments of the Trustees that a delay in the resolution

of the Esgro claim "would place an undue burden" on the reorganization proceedings. (A504). No basis is set forth in the opinion of the District Court supporting that finding. Rather, the District Court disregarded the findings of fact and conclusions of law made by the Bankruptcy Court and arbitrarily directed the commencement of a summary proceeding in the Bankruptcy Court to determine the Trustees' objection to the Esgro claim. (A504). The prejudice and deprivation imposed upon Esgro is patent. The loss of the right to a jury trial and determination of all issues is unwarranted and unjust, particularly in the light of the firm trial date for the commencement of the California Lawsuit in the California Court, only slightly more than one month after the date fixed by the District Court.

This brief is submitted on behalf of Esgro in support of the instant appeal.

Statement of Facts

The facts pertinent to the appeal at bar are as follows:

1. On February 15, 1973, White Front Stores, Inc. and various of its affiliates commenced the California Lawsuit against Esgro, Triumph Sales, Inc. and Francis J. Esgro, in the California Court, asserting 208 purported causes of

action seeking total damages of approximately $379,121.52, under certain license agreements between the parties. (A320, Document No. 21).

2. On March 13, 1973, Esgro filed a petition for an arrangement under Chapter XI of the Bankruptcy Act with the United States District Court for the Central District of California (the "California Bankruptcy Court"). (A20).

3. On March 19, 1973, the California Bankruptcy Court entered an order staying the continued prosecution of the California Action. (A20).

4. Thereafter, White Front Stores, Inc. filed a proof of claim in the Esgro Chapter XI case in the amount of $1,495,628.12, "plus contingent sums." (A320, Document No. 25).

5. On April 29, 1976, the Trustees filed an amended proof of claim with the California Bankruptcy Court in the amount of $1,747,615.11, "plus contingent sums." (A320, Document No. 26).

6. By order dated May 7, 1973 the California Bankruptcy Court authorized Esgro and Sulmeyer to retain counsel to defend the California Lawsuit and to assert any and all claims for affirmative relief. (A320, Document No. 27).

7. On July 27, 1973, Esgro and the other de-

fendants in the California Lawsuit filed their answer to the complaint. (A320, Document No. 22).

8. On July 27, 1973, Esgro and Triumph Sales, Inc. filed a cross-complaint in the California Lawsuit naming White Front Stores, Inc., various of its affiliates and Interstate Stores, Inc. as cross-defendants. The cross-complaint seeks estimated compensatory damages of $30,000,000, plus punitive damages of $5,000,000. (A320, Document No. 23).

9. Thereafter, White Front Stores, Inc. and the other cross-defendants filed an answer to the cross-complaint of Esgro and Triumph Sales, Inc. (A320, Document No. 24).

10. On May 22, 1974, White Front Stores, Inc. and other cross-defendants in the California Lawsuit filed petitions under Chapter XI of the Bankruptcy Act, 11 U.S.C. §§ 701, et seq., with the District Court. (A21, 34-35). On June 13, 1974, the Chapter XI petitions were amended to comply with the provisions of Chapter X of the Bankruptcy Act, 11 U.S.C. §§ 506, et seq. By order dated June 13, 1974, District Judge Cannella approved the Chapter X petitions and thereafter, by order dated June 18, 1974, referred the Chapter X cases, generally, to Bankruptcy Judge Ryan. (A21, 34-35).

11. By order dated June 13, 1974, the District Court stayed the commencement or continuation of all actions against the debtors, including the prosecution of the California Lawsuit. (A21, 35).

the various transactions under con-

12. By order of the Bankruptcy Court dated June 24, 1974, September 1, 1974 was fixed as the last day for the filing of claims against the Chapter X debtors. (A321, Document No. 30).

13. On or about August 30, 1974, Esgro filed a claim in the Chapter X cases against the debtors named as cross-defendants in the California Lawsuit, in the aggregate sum of $38,758,972 (Claim No. 7273A). The claim parallels the assertions made by Esgro in the cross-complaint in the California Lawsuit. (A2-8).

14. On or about April 9, 1976, approximately two years subsequent to the commencement of the Chapter X cases, the Trustees filed an objection to the allowance of the claim of Esgro. (A9-14). The Trustees did not assert any counter-claim against Esgro, but rather, amended the claim filed in the California Bankruptcy Court against Esgro with the intent of having the issues resolved separately by the New York and California Bankruptcy Courts. (A320, Document No. 26).

15. On May 11, 1976, Esgro commenced the adversary proceeding against the Trustees pursuant to Chapter X Rule 10-601, 421 U.S. 1069 (1975) for the primary purpose of modifying the stay of actions order of June 13, 1976 so as to permit the continued prosecution of the California Lawsuit. (A15-29).

16. Bankruptcy Judge Ryan accelerated the trial

date of the adversary proceeding to May 21, 1976 and advised the parties that all pre-trial discovery would be held in suspense pending the determination of the adversary proceeding. (A246-247).

17. On May 21, 1976, the trial of the adversary proceeding commenced before Bankruptcy Judge Ryan. The Bankruptcy Court heard the testimony adduced from three witnesses consisting of the California attorney for Esgro, Joseph R. Crowley, one of the Reorganization Trustees, and the California attorney for the Trustees. The Bankruptcy Court admitted into evidence 31 exhibits. (A318-321).

18. The California attorney for Esgro testified that:

(a) the claims asserted in the complaint and cross-complaint in the California Lawsuit are based upon (i) breach of contract, (ii) fraud and misrepresentation, and (iii) rescission. (A111-114).

(b) many of the witnesses necessary to the defense interposed by Esgro and the prosecution of the cross-complaint reside in California. (A118-120).

(c) the trial of the California Lawsuit would consume at least five weeks. (A204).

(d) completion of necessary discovery would take approximately four months. (A140-141).

19. The California attorney for the Trustees testified that:

(a) it would take approximately fifteen to eighteen months before the California Lawsuit would come to trial unless the California Court advanced the trial date upon application of the parties. (A211-212).

(b) if the application to advance the trial date were granted, there would still be a delay of eight months before the commencement of the trial. (A218).

(c) approximately six to eight weeks of trial would be required to try the issues raised by the complaint and cross-complaint in the California Lawsuit. (A224-225).

(d) many of the issues involved in the complaint and cross-complaint in the California Lawsuit are intertwined. (A225).

20. The Reorganization Trustee, Joseph R. Crowley, testified that:

(a) the disputed and unresolved claims in the Chapter X cases, exclusive of the Esgro claim, aggregated at least $30,000,000 and had not yet been resolved. (A145).

(b) Neither the Chapter X Trustees nor the Bank-

they are going to try cases. This

ruptcy Court had determined whether the claims of institutional lenders to the Chapter X debtors, whose claims aggregate approximately $65,000,000, are secured or unsecured claims. (A164).

(c) the Trustees had not undertaken any real effort to value the assets of the Chapter X debtors for the purposes of formulation of a plan of reorganization under Chapter X of the Bankruptcy Act. (A148).

(d) the process of formulating a plan of reorganization had not been initiated. (A153, 167-169).

(e) the Trustees commenced their examination and review of claims in January, 1975. (A157).

(f) it was not until June or July, 1975 that the Trustees first consulted with their attorneys in respect of the claim of Esgro. (A158).

(g) it was not until April 9, 1976, approximately ten months later, that the Trustees first interposed an objection to the allowance of the claim of Esgro. (A159).

21. On May 26, 1976, after consideration of the evidence, Bankruptcy Judge Ryan granted the relief requested by Esgro in the complaint to the extent that (a) the parties

were directed to make application to the California Court for an order advancing the trial date, (b) authorizing the commencement of discovery, (c) directing the parties to report to the Court "on or before July 8, 1976 for the purpose of advising the Court as to the progress of discovery proceedings and the result of their application to the California Superior Court for an order advancing the trial date of the California [Lawsuit]." (A322-334).

22. On June 4, 1976, a hearing was held before Bankruptcy Judge Ryan on the Trustees' application to expunge the claim of Esgro on the ground that Mr. Francis Esgro had failed to appear for examination at a deposition noticed by the Trustees for June 1, 1976. (A335-345). The application of the Trustees was denied and the Bankruptcy Court directed that all further pre-trial discovery proceed under the auspices and control of the California Court. (A387-388).

23. On June 28, 1976, with the concurrence of counsel for Esgro and the Trustees, the Master Calendar Department of the California Court fixed November 29, 1976, as the date of commencement of the jury trial in the California Lawsuit. (A410).

24. Notwithstanding the prior two attempts to inhibit and restrict the continuation of the California Lawsuit, on July 9, 1976, the Trustees applied to the Bankruptcy Court for an order setting down for trial the

Trustees' objection to the claim of Esgro. (A389-398). This application was heard before Bankruptcy Judge Ryan on July 20, 1976. (A422-481).

25. At the conclusion of the hearing on July 20, 1976, Bankruptcy Judge Ryan stated:

> "THE COURT: I am persuaded that the motion must be, and it is, denied at this time. No cause has been shown to indicate that there should be any relief granted inconsistent with a prior decision on the adversary proceeding. Needless to say the parties are free to come back at any time that there is a significant change in the circumstances of the case." (A479-480).

26. The aforesaid application of the Trustees was denied by order dated July 23, 1976. (A482-486). The order of July 23, 1976 sets forth the findings of fact and conclusions of law made by the Bankruptcy Court. Bankruptcy Judge Ryan found, inter alia:

> "8. No prejudice, harm or disability is incurred by the Reorganization Trustees and the reorganization cases by modification of the automatic stay under Chapter X Rule 10-601 so as to allow the prosecution and trial of the California Action.
>
> "9. The prosecution and trial of the California Action as authorized by the Court is in the interests of justice and convenience of the parties and potential witnesses." (A485).

27. On July 23, 1976, the Trustees filed a notice of appeal from the aforesaid order of the Bankruptcy Court. (A487-488).

28. On August 23, 1976, the appeal was heard on an expedited basis before District Judge Cannella. On September 1, 1976, District Judge Cannella rendered his opinion and order. (A503-506). The District Court found that Bankruptcy Judge Ryan had abused his discretion by modifying the stay of actions and allowing the California Lawsuit to proceed. Accordingly, District Judge Cannella reversed the order of the Bankruptcy Court and, inter alia, withdrew the reference of the Chapter X cases to Bankruptcy Judge Ryan in respect of the Esgro claim and set down the trial of the objection to that claim before him on October 18, 1976. (A504-506).

29. On September 2, 1976, Esgro filed the notice of appeal from the order of the District Court dated September 1, 1976. (A507-508). By order of this Court dated September 7, 1976, the application of Esgro for expedited consideration of the instant appeal was granted.

30. Concurrently with the application to this court for expedited treatment of the appeal, and on September 8, 1976, Esgro applied to the District Court for a suspension and stay of the order of September 1, 1976, which is the subject of this appeal, advising the District Court that Esgro had been informed, by order of this Court dated September 7, 1976, that argument of the appeal would be heard during the week of October 12, 1976. (A509-530). By order of the District Court dated September 17, 1976, the application of Esgro for a suspension and stay was denied.

THE BANKRUPTCY COURT DID NOT ABUSE ITS DISCRETION BY MODIFYING THE STAY AND ALLOWING THE CALIFORNIA LAWSUIT TO PROCEED

A. The Continuation Of A Stay Of Actions In Corporate Reorganization Cases Is Not A Matter Of Right.

Section 116(4) of the Bankruptcy Act, 11 U.S.C. § 516(4), provides the statutory base for the issuance of a stay of actions in connection with Chapter X cases. Pursuant thereto the Reorganization Judge may:

> "* * * enjoin or stay until final decree the commencement or continuation of a suit against the debtor or its trustee * * *".

The Rules of Bankruptcy Procedure applicable to Chapter X cases reinforce and supplement Section 116(4), supra. Thus, Chapter X Rule 10-601, 421 U.S. 1069 (1975), entitled "Petition as Automatic Stay of Actions Against Debtor and Lien Enforcement," provides, inter alia:

> "(a) Stay of Actions and Lien Enforcement. A petition filed under [this chapter] shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor * * *".
>
> "(c) Relief from Stay. On the filing of a complaint seeking relief from a stay provided by this rule, * * * [t]he court may, for cause shown, terminate, annul, modify, or condition such stay * * *".

Clearly, the continuation of a stay granted pursuant to Section 116(4) of the Act, supra, or automatically acquired by virtue of Chapter X Rule 10-601, supra, is not

a matter of right. The modification or termination of a stay falls within the exercise of sound discretion by the bankruptcy court. Foust v. Munson S.S. Lines, 299 U.S. 77 (1936); In re Laufer, 230 F.2d 866 (2d Cir. 1956); Drincup Vendors, Inc. v. Fountain Machines, Inc., 134 F.2d 823 (2d Cir. 1943); In re Adolf Gobel, Inc., 89 F.2d 171 (2d Cir. 1937); In re Murel Holding Corporation, 75 F.2d 941 (2d Cir. 1935); In re Zeckendorf, 326 F.Supp. 182 (S.D.N.Y. 1971).

In the Foust case, supra, the Supreme Court stated the governing principle as follows:

> "The power to stay does not imply that it is to be, or appropriately may be, exerted without regard to the facts. The granting or withholding of injunction is left to the discretion of the court.
>
> * * *
>
> "In reorganization proceedings neither the Act nor any rule of law entitles debtors or trustees as a matter of right to enjoin the trial of actions such as that brought by petitioner. The court is to exercise the power conferred by Subd. (c)(10) according to the particular circumstances of the case and is to be guided by considerations that under the law make for the ascertainment of what is just to the claimants, the debtor and the estate." 299 U.S. at 83. [Emphasis supplied]

In order for the stay to be continued, there must be a clear showing establishing the necessity therefor. Thus, in In re Murel Holding Corporation, supra, Circuit

Judge Learned Hand stated:

> "* * * the stay so authorized, like any other, lies in the court's discretion; if his [the creditor's] hand is to be held up, the debtor must make a clear showing." 75 F.2d at 942.

Similarly, in In re Adolf Gobel, Inc., a reorganization case under former Section 77B of the Bankruptcy Act, the precursor of Chapter X, this court stated:

> "Whether the appellant be allowed to try his suit in the state court or not is a matter within the sound discretion of the court where the 77B proceedings are still pending and that discretion should be exercised by a just balancing of advantage against disadvantage to all concerned." 89 F.2d at 172.

The applicable rule was recently restated by District Judge Marvin E. Frankel in In re Zeckendorf, as follows:

> " *** [A] stay should not be rigidly enforced when no sound reason is shown to require it and where there is good reason for its modification.
>
> * * *
>
> "The problem should preferably have been approached at the outset by treating the stance of the debtor as 'not substantially unlike that of [a suitor] for injunction * * *.'" 326 F.Supp. at 184.

The record before the Bankruptcy Court demonstrates that Esgro sustained its burden of establishing good reason for the California Lawsuit to proceed. At that

point the burden of going forward passed to the Trustees. The Trustees failed to meet that burden. They did not produce any probative evidence to outweigh the demonstration by Esgro that (a) many of the witnesses reside in California (A56, 77-80), (b) complete relief as to the claims and cross-claims involved in the California Lawsuit could only be obtained in the California Court (A164), (c) all of the parties to the California Lawsuit were not before the Bankruptcy Court (A57, 207), (d) California law governed the resolution of the issues between the parties (A56) and finally, (e) that trial by jury was obtainable in the California Court (A140). The Trustees' only argument, to the effect that delay would prejudice the reorganization (A150-151, 154-156), was obviated by the agreement between the attorneys for Esgro and the Trustees and the action of the California Court advancing the trial date of the California Lawsuit to November 29, 1976.

B. Based Upon The Facts Established At The Trial Of The Adversary Proceeding In The Bankruptcy Court, A Modification Of The Stay Was Warranted.

The trial of the adversary proceeding before the Bankruptcy Court established that the continued prosecution of the California Lawsuit was in the best interest of justice and the convenience of the parties and potential witnesses. It is undisputed that Esgro is entitled to a jury trial in the California Court (A140). The importance of preserving the right to trial by jury was highlighted by

the Supreme Court in the Foust case, supra. In that case, it was held that a reorganization court had abused its discretion by refusing to modify a stay. The Supreme Court quoted from its prior decision in Dimick v. Schiedt, 293 U.S. 474 (1934), as follows:

> "Maintenance of the jury as a fact-finding body is of such importance and occupies so firm a place in our history and jurisprudence that any seeming curtailment of the right to a jury trial should be scrutinized with the utmost care." 299 U.S. at 84.

The cross-complaint filed by Esgro in the California Lawsuit asserts claims totalling in excess of $30,000,000. These claims are premised upon averments of fraud and misrepresentation (A320, Document No. 23). The California Lawsuit presents numerous triable issues of fact relating both to liability and damages. The complaint of White Front Stores, Inc. asserts 208 separate causes of action (A320, Document No. 21). At the trial before Bankruptcy Judge Ryan, the uncontradicted testimony established that it would take between five and eight weeks of trial time to present the claims of the respective parties (A204, 225). It is undisputed that the resolution of the issues involves non-bankruptcy law (A111-115). It is also uncontroverted that the issues joined in the California Lawsuit action and cross-action are intertwined and in many respects, identical (A112-114, 164-165, 225). Thus, the interests of

judicial economy, elimination of multiplicity of suits and convenience of the parties and witnesses are best served by the trial of all issues in one forum.

In view of all of the determinative factors as established by the evidence, the decision of the Bankruptcy Court was consistent with the applicable principles of law. In a strikingly similar case, In re Wonderbowl, Inc., 456 F.2d 954 (9th Cir. 1972), the Court of Appeals determined that the trial of certain aspects of a controversy pursuant to the summary jurisdiction of the bankruptcy court was inappropriate and that "[s]ummary jurisdiction may properly be declined, for example, where complete relief cannot be afforded among the interested parties" 456 F.2d at 956. The Court in that case also stated:

> "Plenary litigation may be preferable where important questions turning on nonbankruptcy law are involved. [citing cases]
>
> "Applying [the foregoing principles], we conclude that the proceedings before the referee should have been dismissed or at least stayed pending completion of the trustee's plenary suit in the federal court.
>
> "The trustee's multifarious allegations of fraud raise numerous legal and factual issues as to a whole series of events affecting the present status of the property. Each link in this chain may be crucial to the ultimate validity of claimed interests. A full analysis of

> the various transactions under controlling nonbankruptcy standards is essential. The isolated adjudication of CEI's lien interest could not possibly take adequate account of the complex controversy of which this issue is a part. The same issue is a central part of the plenary suit in federal court. All other contested transactions and some three dozen other affected parties are also before that court, which has unquestioned jurisdiction to decide the entire controversy and to order whatever relief may be appropriate, in equity or at law." 456 F.2d at 956.

See also Gulf Oil Corp. v. Gilbert, 330 U.S. 501 (1947).

In the appeal at bar, it is only through the prosecution of the California Lawsuit that the complex and multi-faceted litigation between the parties can be completely resolved. Consequently, based upon the facts, the modification of the stay as requested by Esgro was and is mandated. The contentions urged by the Trustees that the prosecution of the California Lawsuit will delay the reorganization process is spurious. The testimony of the Trustees established that nothing has been done in the reorganization cases as to (a) valuation of the businesses of the debtors as going concerns (A145-148), an essential prerequisite in Chapter X to plan formulation; (b) the determination of whether $65,000,000 of institutional lender claims are secured or unsecured (A164); (c) resolution of disputed claims other than that of Esgro, aggregating $30,000,000

(A145, 149) and (d) formulation of a plan of reorganization (A153, 167-169).

Further, as stated, the difference in time between the commencement of trial of the California Lawsuit as compared to the date fixed by District Judge Cannella is slightly more than one month. This is hardly a sufficient time gap to effect the severe prejudice which the Trustees desire to impose upon Esgro and the other parties to the California Lawsuit. "Though facility of reorganization is desirable, it is not the sole consideration." In re Beck Industries, 479 F.2d 410, 419 (2d Cir. 1973). The interests of all parties must be considered in light of the pertinent circumstances. The circumstances of the appeal at bar more than justified the action which was taken by the Bankruptcy Court.

C. The Opinion Of The District Court Is Devoid Of Any Basis Which Could Sustain A Finding That The Bankruptcy Court Abused Its Discretion.

Despite the success of the parties in obtaining an advanced trial date from the California Court, at least two months earlier than the best estimate made at the trial of the adversary proceeding, and notwithstanding the agreement between Esgro's California attorneys and the Trustees' California attorneys as to the November 29, 1976 trial date, the Trustees applied to the Bankruptcy Court on July 9, 1976

for an order setting down for trial their objection to the claim of Esgro (A389-398). This was a clear and intentional effort on the part of the Trustees to circumvent the prior determinations of the Bankruptcy Court. The Trustees' application was heard by Bankruptcy Judge Ryan on July 20, 1976 (A422-481). No evidence of whatsoever kind was offered by the Trustees in support of their application. After oral argument at which the attorneys for the Trustees reiterated the oft-repeated contention of delay, Bankruptcy Judge Ryan stated:

> "No cause has been shown to indicate that there should be any relief granted inconsistent with the prior decision on the adversary proceeding" (A479).

On July 23, 1976, the Bankruptcy Court made its order denying the Trustees' application and directing the prosecution and trial of the California Lawsuit in the California Court. (A482-486). On that date, the Trustees filed a notice of appeal to the District Court from the order of Bankruptcy Judge Ryan (A487-488). The Trustees requested an accelerated hearing before the District Court and District Judge Cannella at the insistence of Esgro set down a hearing for August 3, 1976. At that hearing and prior to the transmittal of the record on appeal, District Judge Cannella indicated a clear and unequivocal disposition to reverse the Bankruptcy Court. At the outset, the District Judge stated:

"THE COURT: I know about this matter and I know what it is about now, actually. I don't know what the briefs are going to do to help me any more than that. I am aware of what it is about. I have lived with this case a long time. My office has too." (A498-499).

In response to the desire of Esgro to have the opportunity to present its case and submit a memorandum of law relative thereto, the following transpired:

"THE COURT: There is nothing to know. You have a claim for 33 million plus five punitive damages for whatever it is, 38 million, and the question is should it proceed in California or here, and essentially that is what is involved.

"What else are you going to talk about?

"[Counsel for Esgro]: We are going to talk about whether or not, in light of all circumstances, Judge Ryan abused his discretion in modifying --

"THE COURT: I just reversed him only recently, so I am not interested in what Judge Ryan thinks or doesn't think about the matter. What I am interested in is expediting this matter and getting this report in that the Trustee must hand in with some expedition. That is what I am interested in.

"[Counsel for Esgro]: With joint agreement of California counsel for both parties a trial date of September [sic] 29th --

"THE COURT: I couldn't care less about what they agreed. I have the obligation of this. They don't have the obligation. They are adversaries. They want to accomplish some purpose. I only want to accomplish one purpose, to get this thing expeditiously done, well done and that is it. I have sat on some of those dates

> they are going to try cases. This is my 28th year now. I didn't come in the door yesterday. I have seen some of these things where I used to hold my breath, the Supreme Court is going to decide, they heard the argument, I have sat on some of those for six, seven months. Upstairs they sit on it 20 months. I am not going to sit around and watch people twiddle their thumbs and contemplate their navels. I am not deciding it. I am only telling you what my interests are." (A499-501).

On September 1, 1976, District Judge Cannella rendered his opinion and order (A503-506). The District Court found the commission of an abuse of discretion by the Bankruptcy Court and reversed the order of July 23, 1976 (A504). It reinstated the stay against the continued prosecution of the California Lawsuit (A504). The opinion below, which is devoid of any citation of legal authority, is totally inadequate to set aside or reverse the findings of fact and conclusions made by the Bankruptcy Court. The only basis upon which the District Court premised its reversal of the Bankruptcy Court is that:

> "Even a minor delay at this juncture would place an undue burden on these reorganization proceedings." (A504).

On that basis and solely that basis, the District Court undertook to overrule the unequivocal policies and principles enumerated by the Supreme Court and other courts in the cases cited above. Apparently the District Court concluded that a time difference of slightly more than one

month as to the commencement of trial was sufficient to disregard the compelling interest and determinative factors which the Bankruptcy Court sought to preserve and evaluate. It is respectfully submitted that the District Court did not seriously consider the evidence submitted to the Bankruptcy Court.

Moreover, the District Court ignored the findings of fact made by the Bankruptcy Court in the order of July 23, 1976 that (a) "no prejudice, harm or disability is incurred by the Reorganization Trustees and the reorganization cases as a result of the modification of the automatic stay under Chapter X Rule 10-601 * * *" and (b) "the prosecution and trial of the California [Lawsuit] * * * is in the interest of justice and convenience of the parties and potential witnesses." (A485). It is submitted that the findings of fact made by the Bankruptcy Court may not be set aside on appeal unless "clearly erroneous". Bankruptcy Rule 810, 411 U.S. 1090 (1972) made applicable to Chapter X cases by Chapter X Rule 10-801 provides:

> "Upon an appeal the district court may affirm, modify, or reverse a referee's judgment or order, or remand with instructions for further proceedings. The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge the credibility of the witnesses."

The foregoing Rule is, in effect, a codification

of the principle long stated by the courts. In re G.E.C. Securities, Inc., 223 F.Supp. 861, 863 (S.D.N.Y. 1963), aff'd, 331 F.2d 655 (2d Cir. 1964); Simon v. Agar, 299 F.2d 853 (2d Cir. 1962). As the United States Supreme Court observed in Cone v. West Virginia Pulp & P. Co., 330 U.S. 212, 216 (1946), a reviewing court should give due weight to the "judgment in the first instance of the Judge who saw and heard the witnesses and has the feel of the case." On the basis of the record it cannot be concluded that the Bankruptcy Court's findings are "clearly erroneous." Consequently, the District Court erred in reversing the order of July 23, 1976 and reinstating the stay of the California Lawsuit (A504).

District Judge Cannella has ignored the judicious manner in which Bankruptcy Judge Ryan exercised his control over the proceedings in the Bankruptcy Court. Bankruptcy Judge Ryan explicitly stated that should a trial in the California Court be substantially delayed or should Esgro be dilatory in connection with the California Lawsuit then he would reinstate the stay and set the matter down for trial of the objection to the allowance of the claim of Esgro. On May 26, 1976, the Bankruptcy Judge stated:

> "If anybody should drag their heels, they can come back here to reinstate the stay and set down the trial of the objections to the claim.
>
> * * *

"THE COURT: They [the Reorganization Trustees] have the whip and can come in at any time and ask to have the stay reinstated, because you [Esgro] are not proceeding with due dispatch. It seems to be this simple." (A286, 294).

Notwithstanding the effort on the part of the Bankruptcy Court to balance the respective interest of the parties and to assure fair treatment, the District Court without any real explanation arbitrarily reinstated the stay. As a consequence, a piece of a complex litigation is to be summarily tried before the District Judge in charge of the administration of the reorganization case rather than before an independent court with no relationship to the reorganization case or the Trustees appointed therein. The result does not enhance or further the evenhanded disposition of justice in bankruptcy cases. The interest of all parties would be best served by the continued prosecution of the California Lawsuit as allowed by the Bankruptcy Court.

CONCLUSION

The order of the District Court should be reversed and the continued prosecution of the California Lawsuit allowed in accordance with the order of the Bankruptcy Court.

Respectfully,

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Harvey R. Miller,
Bruce R. Zirinsky,
Lawrence Mittman,

Of Counsel.

Index No. 76-5034 *Year 19*

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In re
INTERSTATE STORES, INC., et al.,
Debtors,
IRVING SULMEYER, as Receiver for the Estate of ESGRO, INC., a Debtor in Chapter XI,
Plaintiff-Respondent-Appellant,
-against-
JOSEPH R. CROWLEY and HERBERT B. SIEGEL, as Reorganization Trustees for WHITE FRONT STORES, INC., et al.,
Defendants-Appellants-Appellees.

AFFIDAVIT OF SERVICE BY HAND

Attorneys for **WEIL, GOTSHAL & MANGES**
Plaintiff-Respondent-Appellant

767 FIFTH AVENUE
BOROUGH OF MANHATTAN, NEW YORK, N.Y. 10022
(212) 758-7800

To:

Attorney(s) for

Service of a copy of the within *is hereby admitted.*

Dated:

.....

Attorney(s) for

PLEASE TAKE NOTICE

Check Applicable Box

☐ NOTICE OF ENTRY *that the within is a (certified) true copy of a entered in the office of the clerk of the within named court on* *19*

☐ NOTICE OF SETTLEMENT *that an Order of which the within is a true copy will be presented for settlement to the Hon. one of the judges of the within named Court, at*
on *19* *, at* *M.*

Dated:

WEIL, GOTSHAL & MANGES

Attorneys for

767 FIFTH AVENUE
BOROUGH OF MANHATTAN, NEW YORK, N.Y. 10022

To:

Attorney(s) for

N 912 CL

STATE OF NEW YORK, COUNTY OF ss:

I, the undersigned, am an attorney admitted to practice in the courts of New York State, and

Check Applicable Box

☐ Attorney's Certification — certify that the annexed has been compared by me with the original and found to be a true and complete copy thereof.

☐ Attorney's Verification by Affirmation — say that: I am the attorney of record, or of counsel with the attorney(s) of record, for . I have read the annexed know the contents thereof and the same are true to my knowledge, except those matters therein which are stated to be alleged on information and belief, and as to those matters I believe them to be true. My belief, as to those matters therein not stated upon knowledge, is based upon the following:

The reason I make this affirmation instead of is

I affirm that the foregoing statements are true under penalties of perjury.
Dated:

(Print signer's name below signature)

STATE OF NEW YORK, COUNTY OF ss:

being sworn says: I am

Check Applicable Box

☐ Individual Verification — in the action herein; I have read the annexed know the contents thereof and the same are true to my knowledge, except those matters therein which are stated to be alleged on information and belief, and as to those matters I believe them to be true.

☐ Corporate Verification — the of a corporation, one of the parties to the action; I have read the annexed know the contents thereof and the same are true to my knowledge, except those matters therein which are stated to be alleged on information and belief, and as to those matters I believe them to be true.

My belief, as to those matters therein not stated upon knowledge, is based upon the following:

Sworn to before me on , 19

(Print signer's name below signature)

STATE OF NEW YORK, COUNTY OF ss:

age and reside at being sworn says: I am not a party to the action, am over 18 years of

On , 19 , I served a true copy of the annexed in the following manner:

Check Applicable Box

☐ Service By Mail — by mailing the same in a sealed envelope, with postage prepaid thereon, in a post-office or official depository of the U.S. Postal Service within the State of New York, addressed to the last known address of the addressee(s) as indicated below:

☐ Personal Service — by delivering the same personally to the persons and at the addresses indicated below:

Sworn to before me on , 19

(Print signer's name below signature)

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In re	:	
INTERSTATE STORES, INC., et al.,	:	
Debtors,	:	76-5034
IRVING SULMEYER, as Receiver for the Estate of ESGRO, INC., a Debtor in Chapter XI,	:	AFFIDAVIT OF SERVICE BY HAND
Plaintiff-Respondent-Appellant,	:	
-against-	:	
JOSEPH R. CROWLEY and HERBERT B. SIEGEL, as Reorganization Trustees for WHITE FRONT STORES, INC., et al.,	:	
Defendants-Appellants-Appellees.	:	

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

EDWARD C. WALLACE, being duly sworn, deposes and says:

1. I reside at 64-18 99th Street, Rego Park, New York 11374, I am over 18 years of age and I am not a party to the within proceedings.

2. On September 22, 1976, I personally delivered and served:

(a) Two copies of the brief in the above-captioned case upon Lester Yassky, Esq., Shea, Gould, Climenko & Casey, 330 Madison Avenue, New York, New York;

(b) Two copies of the brief and one copy of the appendix in the above-captioned case upon Richard Totter, Esq., Zalkin, Rodin & Goodman, 750 Third Avenue, New York, New York; and

(c) Two copies of the brief and one copy of the appendix in the above-captioned case upon Merryl Weiner, Esq., Securities and Exchange Commission, 26 Federal Plaza, New York, New York.

Edward C Wallace

Edward C. Wallace

Sworn to before me this
22nd day of September, 1976

David C. Unger

Notary Public

DAVID C. UNGER
Notary Public, State of New York
No. 31-4600333
Qualified in New York County
Commission Expires March 30, 1978